DEPARTMENT OF STATE REVENUE

Revenue Ruling #2015-21ST
March 3, 2016

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the department's official position concerning a specific issue.

ISSUES

Sales and Use Tax - Vehicle Protection Plan

Authority: IC 6-2.5-1-11.5; IC 6-2.5-2-1; IC 6-2.5-3-2; IC 6-2.5-4-1; IC 6-2.5-4-15; Sales Tax Information Bulletin #2 (January 2013)

A company ("Taxpayer") is seeking a determination regarding whether the sale of an extended service contract by the Taxpayer in connection with the sale of a motor vehicle is subject to Indiana sales tax.

STATEMENT OF FACTS

Taxpayer is an Arizona company. It operates in multiple states as a seller of used vehicles. Taxpayer provides the following information regarding its business:

> The Taxpayer is a used car retail dealer registered in Indiana with the Department for sales and use tax. In connection with its motor vehicle sales transactions, the Taxpayer offers for sale an optional extended service contract that is administered by a third party and covers the costs associated with the repair or replacement of malfunctioning parts. The service contract is separately invoiced to the customer. The Taxpayer collects and remits Indiana sales tax on sales of this service contract, and has done so since commencing sales of such contracts in Indiana in late 2013.

DISCUSSION

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC 6-2.5-2-1(b). Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC 6-2.5-3-2(a).

IC 6-2.5-4-1 defines "retail transactions" stating in part as follows:

> (a) A person is a retail merchant making a retail transaction when he engages in selling at retail.
> (b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business he:
> (1) acquires tangible personal property for the purpose of resale; and
> (2) transfers that property to another person for consideration.
> (c) For purposes of determining what constitutes selling at retail, it does not matter whether:
> (1) the property is transferred in the same form as when it was acquired;
> (2) the property is transferred alone or in conjunction with other property or services; or
> (3) the property is transferred conditionally or otherwise.

Further, IC 6-2.5-4-15 provides that "[a] person is a retail merchant making a retail transaction when the person sells tangible personal property as part of a bundled transaction."

IC 6-2.5-1-11.5 defines "bundled transaction" as follows:

> (b) "Bundled transaction" means a retail sale of two (2) or more products, except real property and services to real property, that are:
> (1) distinct;

(2) identifiable; and
(3) sold for one (1) nonitemized price.
(c) The term does not include a retail sale in which the sales price of a product varies, or is negotiable, based on other products that the purchaser selects for inclusion in the transaction.
(d) The term does not include a retail sale that:
(1) is comprised of:
(A) a service that is the true object of the transaction; and
(B) tangible personal property that:
(i) is essential to the use of the service; and
(ii) is provided exclusively in connection with the service;
(2) includes both taxable and nontaxable products in which:
(A) the seller's purchase price; or
(B) the sales price;
of the taxable products does not exceed ten percent (10%) of the total purchase price or the total sales price of the bundled products; or
(3) includes both exempt tangible personal property and taxable tangible personal property:
(A) any of which is classified as:
(i) food and food ingredients;
(ii) drugs;
(iii) durable medical equipment;
(iv) mobility enhancing equipment;
(v) over-the-counter drugs;
(vi) prosthetic devices; or
(vii) medical supplies; and
(B) for which:
(i) the seller's purchase price; or
(ii) the sales price;
of the taxable tangible personal property is fifty percent (50%) or less of the total purchase price or the total sales price of the bundled tangible personal property.
The determination under clause (B) must be made on the basis of either individual item purchase prices or individual item sale prices.

The question is whether Taxpayer's service contract would qualify as an "optional maintenance contract" or an "optional warranty contract." As explained in Sales Tax Information Bulletin #2 (January 2013), the Department treats "optional maintenance contracts" and "optional warranty contracts" differently. "Optional maintenance contracts" are subject to Indiana sales and use tax, whereas "optional warranty contracts" are not. Sales Tax Information Bulletin #2 provides an explanation for the difference between an "optional maintenance contract" and an "optional warranty contract" as follows:

> Maintenance contracts generally meet the definition of bundled transactions under IC 6-2.5-1-11.5 and are subject to sales tax on that basis. **The determination as to whether a contract is a maintenance contract is not necessarily based on the particular title of or language used in the contract. Instead, the determination is based on the substantive provisions contained in the contract**. **An explicit guarantee that tangible personal property will be provided under the contract is not required. What is important is that both the customer and the service provider are aware at the time the contract is executed that consumable items will be provided under the contract.** However, the amount of tangible personal property supplied under the contract must be more than a de minimis amount. As a rule, the seller's purchase price or the sales price of the taxable items provided under the contracts must exceed 10% of the total purchase price or the total sales price of the bundled products.
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> For purposes of this bulletin, a "warranty contract" means a contract that acts like insurance against future potential repair costs, including extended service contracts. As with maintenance contracts discussed previously, the determination as to whether a contract is a warranty contract is not necessarily based on the particular title of the contract or language used therein. Instead, the determination is based on the substantive provisions contained in the contract. **Under a warranty contract, neither the seller nor the purchaser is certain at the time the contract is signed whether any tangible personal property will be provided under the terms of the contract**. **Unlike a maintenance contract, the replacement of consumable items is not included under a warranty contract**.

> Optional warranty contracts are not implicated by the bundled transaction provisions in IC 6-2.5-1-11.5 because the warranty contracts do not meet the definition of a bundled transaction. The sale does not include the sale of two or more products because, under the warranty contract, there may never be any parts or services provided to the customer. Accordingly, the sales of optional warranty contracts are exempt from sales tax. However, the provider of the service must pay sales or use tax on the cost of all taxable items used under the contract, based on the acquisition cost of the service provider, which does not include a deductible collected from the customer. If the service provider charges a separate amount for parts or other taxable items, the provider should purchase the items exempt for resale and charge sales tax to the customer. If the service provider charges one non-itemized amount for the service and any tangible personal property transferred under the contract, the provider must self-assess and remit use tax on its purchase price of the property. (**Emphasis added**)

Taxpayer contends that its service agreement is an optional warranty contract. Taxpayer describes the service contract in more detail as follows:

> Certain consumable tangible personal property may be provided to the purchaser under the service contract ("Covered Parts," as defined in the section of the contract with the same name). Covered Parts are provided to the purchaser under the service contract, but only if and when a qualifying event occurs (a "Breakdown," as defined in the Definitions section of the contract). In the event Covered Parts are provided to the purchaser following a Breakdown, the third-party administrator reimburses either the provider of the Covered Parts or the purchaser of the service contract.

Taxpayer concludes that the service contract is an optional warranty contract rather than an optional maintenance contract because "neither the seller nor the purchaser is certain at the time the contract is signed whether any tangible personal property will be provided under the terms of the contract," as provided in Sales Tax Information Bulletin #2. After reviewing the service contract, the Department concurs that it is indeed an "optional warranty contract," as it "acts like insurance against future potential repair costs, including extended service contracts." Only in the event of a "breakdown" of a "covered part" is a customer eligible for any repair or replacement part. As stated in the contract:

> If a covered Breakdown of Your Vehicle occurs during the term of this Contract, Provider, through Administrator, will:
> • Pay You or the repairer, for repair or replacement, as the Administrator deem appropriate, of the Covered Part(s) which caused the Mechanical Breakdown if You have met Your obligations as described in this Contract and if the Breakdown is not excluded under the exclusions section of this Contract. Replacement parts can be of like kind and quality. This may include the use of new, remanufactured or used parts as determined by the Administrator.

There is no guarantee that tangible personal property will be provided or even an assumed provision of tangible personal property. Therefore, the "optional extended service contract" is not subject to sales and use tax. However, as mentioned in the Sales Tax Information Bulletin #2, Taxpayer must pay sales or use tax on the cost of all taxable items used under the contract, unless they're purchased for resale to Taxpayer's customers, in which case Taxpayer could purchase the parts exempt but charge sales tax to Taxpayer's customers for the parts.

RULING

Taxpayer's "optional extended service contract" is an "optional warranty contract," and therefore not subject to Indiana sales and use tax.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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